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As the Economy Falters, So Do State Budgets

By Jennifer Steinhauer

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Programs for the elderly are being slashed in Maine. Government jobs are being eliminated in New Jersey. Prison construction has been put off in Virginia. Some schools in California will end their music programs.

About half of the state legislatures nationwide are scrambling to plug gaps in their budgets, shot through by rapid declines in corporate and sales tax revenue, distressed housing markets and a national economy on the verge of a recession.

Many states are reporting their largest budget shortfalls since the recessions of 2001 and 1991-2. In some states where tax increases are generally anathema, including Maryland and Kentucky, governors are looking to raise some levies.

“It is not just the standard downturn where unemployment rises for a while, income tax and sales tax revenues are weak, and ultimately the economy recovers,” said Iris Lav, the deputy director of the Center on Budget and Policy Priorities, a liberal research group in Washington that tracks state budgets.

Ms. Lav pointed to a confluence of factors — including weak consumer spending, high energy prices, dropping housing values and growing foreclosure rates — that suggest states will face a protracted struggle to keep their budgets afloat.

“This all will make it harder to recover,” she said.

As of last week, at least 25 states were expecting budget shortfalls for the 2009 fiscal year, according to the budget center, findings that are consistent with other state roundups and an informal phone survey by The New York Times. It is the largest number since 2002, when in the aftermath of the 2001 recession 37 states were forced to cut their budgets.

Many of the states this year owe their problems to stark declines in tax revenues after an implosion in housing markets. California is looking to fill a \$14.5 billion hole for its next fiscal year, and Arizona’s \$1.8 billion budget gap is 16 percent of its general fund, the largest percentage in the nation.

In New York, the incoming governor, David A. Paterson, a Democrat who takes over Monday for Eliot Spitzer, faces the immediate task of controlling state spending and finding revenues in the face of a projected \$4.4 billion budget gap.

Florida has seen its sales tax revenue decline for two straight fiscal years, the first time officials there recall that happening, the result of a collapsing housing market that has homeowners spending less. The state, which has no income tax, relies heavily on sales taxes for its state programs.

Other states have their own problems. Kentucky has its largest budget crisis in state history, sparked by the movement of manufacturing jobs overseas. New York's budget has felt the wounds delivered by its mercurial friend Wall Street.

Some states are filling holes in their current budgets as they look toward the next fiscal year — or in the case of states that operate on two-year budget cycles, in the face of dire predictions about future revenues.

In most cases, states have moved to cut state spending, particularly in education. Ms. Lav said that eight states are cutting into the budgets for higher education, and nine states are cutting into their financing for primary and secondary education. (There is some overlap between those two groups.)

Delaware will not finance new school construction, and in Arizona, where school enrollment continues to explode, the Legislature, which wants to continue to pay cash to build schools, is fighting the governor, who would prefer to borrow for that construction in light of the state's woes.

"Most places don't have to build a school every year," said Barrett Marson, the spokesman for the Arizona House Republicans. "We have to."

To help close a \$600 million budget gap in Virginia, the state made hundreds of thousands of dollars in cuts at universities, including dorm cleaning staff, library budgets and graduate assistantships. (The governor wrote the state a check, giving back 5 percent of his salary, to help balance the books.)

In California, Gov. Arnold Schwarzenegger's proposed budget for 2008-9 includes a \$4.4 billion cut in public education, the largest ever considered in the state. School districts, preparing for next year's budgets, are already contemplating cuts to their staff. In the Alameda school district in Northern California, trustees voted to reduce the \$83.7 million budget by cutting \$200,000 to the sports programs, eliminating music programs for all children below fourth grade and increasing class sizes in ninth grade to an average of 29 students, up from 20.

Ballooning health care costs have vexed many states over the last decade, and nine are now trimming their Medicaid programs, particularly programs for children.

Those cuts range from large — in New York, for example, Mr. Spitzer had been contemplating cuts of \$1 billion in health care spending — to small, as in Rhode Island, where Gov. Donald L. Carcieri wants to take roughly 2,000 children of illegal immigrants off the Medicaid rolls. In the last recession, nearly 35 states cut eligibility for public health programs, causing well over one million people to lose health coverage, according to the Center on Budget and Policy Priorities.

In Delaware, the state is looking to fill \$50 million to \$75 million in shortfalls. “The economic climate is deteriorating here,” said Jennifer Davis, the director of the State Office of Management and Budget.

“Good state budget managers kind of manage their budgets like a household,” Ms. Davis said. “When gas and milk costs go up, there are only so many ways to solve it. You don’t eat out, you stop going to movies, you cut out the discretionary stuff.”

Other states are biting deeply into social service programs. In Maine, the state is facing a \$190 million shortfall for its current budget. It is starting with about \$65 million in proposed cuts to social services.

There has already been a reduction in money for home-based services for the elderly, a lowered Medicaid reimbursement rate for hospital-affiliated physicians, a freeze in enrollment to the state’s Medicaid program for some low-income adults, and a cut in reimbursement rates for foster parents. “It’s a pretty big problem,” said Roger Q. Fenn, the spokesman for Maine’s senate president, Beth Edmonds.

Also in Maine, the judicial branch anticipates a three- to six-week period of delaying payments to vendors and lawyers, coinciding with the term ending the fiscal year.

“Lawyers have been very patient in dealing with us on this,” said Leigh Saufley, the state’s chief justice.

Many states are cutting government employees or trimming raises. “A 5 percent pay increase for teachers and state employees is now down to 3 percent,” said Cathy Holland-Smith, the manager of budget and policy for the Idaho Legislature. “And spending for new programs is down, from \$28.5 million to \$7.5 million.”

While most states are looking to address their budget anguish through cuts, tax increases are occasionally broached.

The Maryland Legislature made the difficult choice of increasing the state’s sales tax to 6 percent from 5 percent, raising its corporate taxes to 8.25 percent from 7 percent, and bumping the state’s cigarette tax to \$2 per pack from \$1. In Kentucky, the governor has proposed a 70-cent increase on cigarette taxes, raising it to \$1 a pack, and Mr. Schwarzenegger in California has spoken vaguely about closing “tax loopholes” in his state.

Raising taxes “hasn’t been discussed specifically,” Mr. Fenn said. “What has been mentioned is possible sales tax increases and other fees.” Maine’s sales tax is 5 percent.

But not all is bleak. States that produce oil have are having a better time, as are states with strong agricultural economies, like Kansas, where revenues for the next fiscal year will increase 2.7 percent and financing for schools is going to be increased, officials said.

It also helps to live in a state people have not been flocking to.

For example, North Dakota, seven months into its fiscal year, is \$90 million ahead of official projections, said Pam Sharp, director of the State Office of Management and Budget. “There is no shortfall at all,” Ms. Sharp said. “We’re at 13 percent ahead of forecast.”

She added: “We haven’t experienced the prime mortgage turnover. The states that are seeing that shortfall in sales taxes are states that have been hit pretty hard with the mortgages.”

Ray Scheppach, the executive director of the National Governors Association, said things were likely to worsen over all. “The major impact on states is the year after a recession stops or the following year,” Mr. Scheppach said, because personal income taxes tend to lag economic recoveries. “It is really sort of the worst as you begin to recover.”